January 4, 2001

Office of Policy
Office of Economic, Electricity and
Natural Gas Analysis
PO-21
U.S. Department of Energy
Forrestal Building
Room 7H-034
1000 Independence Avenue, S.W.
Washington, D.C. 20585

Attention: Electric Reliability Comments

Dear Sir or Madam:

Enclosed please find a signed original and three copies of the Comments of the Alliance for Competitive Electricity in response to the Department=s Notice of Inquiry published in the November 20, 2000 *Federal Register* (65 *Fed. Reg.* 69753). A computer diskette containing the comments in WordPerfect is also enclosed.

A copy of the Alliance comments has also been filed with the Department electronically.

If there are any questions regarding these comments, or if you need additional information, please do not hesitate to contact me.

Sincerely,

Randall E. Davis
Executive Director and Counsel

Enclosures

BEFORE THE
UNITED STATES DEPARTMENT OF ENERGY
WASHINGTON, D.C.

Interstate Electric Transmission System;	)	
	)	Notice of Inquiry
Electric Reliability Issues	)	

COMMENTS OF THE ALLIANCE FOR COMPETITIVE ELECTRICITY

I. Introduction

These comments are submitted on behalf of the Alliance for Competitive Electricity (AAlliance@). The Alliance is an ad hoc group of 10 small and large electric utilities located throughout the U.S. that was formed to work for the enactment of comprehensive federal electric industry restructuring legislation.[1] Members of the Alliance today have utility operations in some 20 states and non-utility operations in nearly all 50 states.

The Alliance commends the Department for its focus on preserving the reliability of the bulk power system. We share the Department=s concern that, with the transition to competitive electricity markets, the system of voluntary reliability self-regulation by the electricity industry, which has worked in the past, may not be adequate to meet the growing demands placed on the bulk power system. For this reason, the Alliance supports the establishment of an electricity reliability regime featuring enforceable reliability rules, coupled with a regulatory structure that encourages infrastructure development and operational initiatives to improve reliability.

With the advent of increased wholesale and retail competition, hundreds of new market entrants are today involved in the generation and sale of electricity. The existing industry reliability system, relying upon the voluntary cooperation of incumbent electric utilities and

[1]Members of the Alliance are: Central Maine Power Company; Detroit Edison Company; Dominion Resources, Inc.; Duke Energy Corp.; Entergy Corporation; GPU, Inc.; National Grid, USA; Public Service Electric and Gas Company; Public Service Company of New Mexico; and Xcel Energy.

institutions, simply was not designed with this new marketplace in mind. There is a consensus that a reliability code of conduct enforced by an industry self-regulatory organization with oversight by the Federal Energy Regulatory Commission (AFERC@), extending to all market participants and all owners of transmission, should replace the existing voluntary system designed for a different era.

The means to achieve this objective, we believe, is through federal legislation. While FERC has clear authority to authorize economic incentives to improve reliability, its authority under existing law to prescribe mandatory and enforceable reliability rules is unclear. FERC heretofore has not regulated reliability directly.

Passage of reliability legislation alone, however, will not address the critical issue of impediments and disincentives to needed generation and transmission infrastructure enhancements, which have the potential to degrade the continued reliability of our power supply. Any potential action on reliability rules must be coupled with other common sense initiatives and actions if the continuing availability of electric power is to be assured for consumers. Comprehensive restructuring legislation that addresses reliability as well as transmission siting, FERC jurisdiction, reform of the Public Utility Regulatory Policies Act, repeal of the Public Utility Holding Company Act and others key issues, is necessary. Given the growing threat to power reliability, as demonstrated all too clearly by the recent developments in California, comprehensive action to address electricity market and reliability issues should be a priority for the 107th Congress.

II. Enforceable Reliability Rules Must Be Coupled With Other Measures.

A number of factors contribute to the heightened concern over reliability. Most important, investment in transmission infrastructure (*e.g.*, lines, poles and transformers) has not kept pace with the ever increasing demands being placed on it. For example, Energy Information Administration data show that between 1990 and 1996, there was a decline of 5% in transmission investment relative to total energy production. Data compiled by the North American Electric

Reliability Council (ANERC@) also indicate a 16% decline in miles of transmission lines per MW of summer demand for the 1989-1997 period. Further declines in transmission capacity also have been projected.[2]

Declining infrastructure investment is understandable, given the legislative and regulatory changes and uncertainty that have surrounded the electricity industry over the past five years. Since 1995, the industry has had to grapple with FERC Orders No. 888 and 889, which were designed to achieve the functional separation of transmission and other electric utility assets, and FERC Order No. 2000 calling for the establishment of regional transmission organizations. Some 24 states and the District of Columbia also have acted to begin the functional or structural unbundling of transmission and retail customer choice for electricity, and all the while, Congress has had restructuring legislation under consideration. There has also been a good deal of regulatory wrangling between federal and state regulators over who will exercise jurisdiction over transmission facilities and services. To exacerbate this regulatory uncertainty, as the Department of Energy=s Power Outage Study Team (APOST@) noted, Ain many cases, state and federal regulatory polices are not providing adequate incentives for utilities to maintain and upgrade facilities to provide an acceptable level of reliability.@[3] To make matters worse, some state laws have capped or frozen retail rates, further calling into question whether the costs of new transmission facilities will be recovered. Given this regulatory and legislative landscape, it is hardly surprising that many utilities naturally are reluctant to make capital investments in assets that may never be recovered.

Second, the number of daily, and even hourly, transactions the grid is being asked to process and schedule is increasing dramatically. A transmission grid designed to serve native load customers in an era where relatively few transactions among relatively few market participants were conducted is now being asked to accommodate a far different market structure.

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[2] *See* AMaintaining Transmission Adequacy in the Future,@ The Electricity Journal, at 62-3 (November 1999).

[3] *See* POST Interim Report at S-2 (January 2000).

Consequently, hardware, software, and human management systems are being strained as never before.

The Final POST report, in endorsing creation of mandatory reliability standards, acknowledged the importance of a comprehensive approach:

> Industry-led voluntary reliability standards for bulk power system operation and planning have worked effectively since their inception. These efforts are the logical and appropriate starting point to change from voluntary to mandatory standards. The federal government should continue its support for this evolutionary process by authorizing the creation of a self-regulated reliability organization with federal oversight to ensure compliance with reliability standards. **However, this effort should not be undertaken in isolation. It must be treated as an integral element of a comprehensive plan for restructuring the industry. A piecemeal approach that treats reliability in isolation would compromise reforms needed in other arenas linked to reliability (e.g., more efficient markets, regional operations of grids).**

POST Final Report at 21 (March 13, 2000)(emphasis supplied).

The Alliance concurs. Passing any reliability legislation alone cannot assure reliability or fully address the pervasive regulatory and legislative disincentives now confronting the electric industry, and cannot solve the pressing need to encourage the construction and improvement of infrastructure -- the fundamental bedrock from which reliability arises. What is needed is a clearer statutory framework for the electric industry of the future, including incentives for increased investment in transmission and other infrastructure. Congress, through comprehensive legislation, can provide this.

For example, there is continuing debate over whether the States or the FERC have, or should have, authority to set retail transmission rates, both the rates for the transmission component of bundled retail sales and the rates for the transmission component of unbundled retail sales. The States have exercised this jurisdiction historically. Recently FERC has asserted greater jurisdiction over the national transmission grid, and the courts have upheld FERC=s view.

Moreover, even under Order 888, FERC lacks jurisdiction over about one quarter of the

U.S. transmission grid, namely, that portion owned by entities such as municipal utilities, co-operatives, Power Marketing Administrations and the TVA. Any attempt to promulgate reliability regulations under FERC=s existing authority could not bind these non-jurisdictional entities, whose participation is so vital to a comprehensive reliability system. Even if legislation were to bring these entities within the scope of a new reliability regime, there would remain the problem of different transmission rules for different players that would leave the nation with a balkanized grid that is bound to be less reliable.

Finally, it may be time to consider new jurisdictional approaches to the siting of new transmission lines, and to reconsider the need for a federal role, especially as transactions over the grid become increasingly regional and interstate in nature. Unless new transmission facilities can be sited in an expeditious fashion, reliability inevitably will suffer. The events of recent weeks in California provide dramatic evidence of the interconnectedness of these issues, and the reasons why a piecemeal approach ultimately will not guarantee a reliable and efficient electricity system.

III. Comprehensive Legislative Action Is Necessary to Assure Reliability Is Maintained.

The only way to satisfy fully the need for a mandatory reliability system in a timely manner is through enactment of federal legislation. This is the conclusion reached by the Electric System Reliability Task Force of the Secretary of Energy Advisory Board in 1998, which determined then that federal legislation is needed to clarify the Commission=s authority to enforce reliability rules. In addition, FERC=s actions demonstrate the limits traditionally observed by the Commission with respect to reliability issues. The Commission=s policy has been to defer to the actions of regional and national industry reliability organizations in the establishment of reliability standards. FERC has confined its focus to those areas that directly affect the Commission=s responsibilities under the Federal Power Act (AFPA@) for the economic regulation of the rates, terms and conditions of wholesale electricity sales and services.

A. The View that Federal Legislative Action Is Needed to Provide for Mandatory Reliability Rules Is Shared Widely.

The Interim Report of the Task Force on Electric-System Reliability of the Secretary of Energy Advisory Board (AESR Task Force@) recommended in July 1997 that federal legislation clarify FERC=s authority to approve and oversee the operation of an electric reliability organization.[4] Subsequently, in November 1997, the Task Force adopted a position paper, AMaintaining Bulk-Power Reliability Through Use of a Self-Regulating Organization.@ In this paper, the Task Force concluded that:

> Most participants in and observers of the electricity industry agree that the voluntary system must be replaced with one that requires compliance with enforceable, non-discriminatory reliability rules applicable to all entities participating in the electricity market. This requires federal legislative authority.

See ESR Task Force Final Report at 65. The position paper observed that it is Anot clear@ whether FERC has sufficient statutory authority to enforce reliability rules established by NERC.[5] In light of these concerns, the Task Force recommended in its final report in 1998 that Congress adopt legislation to clarify FERC enforcement authorities, and to enable the Commission to approve a national self-regulating organization to establish electric reliability

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[4]*See* Appendix A to ESR Task Force Final Report at 61 (September 29, 1998). In describing FERC=s role, the interim report noted that FERC implements policies to assure that owners and operators of bulk power transmission facilities behave in a nondiscriminatory manner. *Id*. at 59. The report continued that A[h]istorically, the FERC has not had to involve itself with regulating reliability functions. Increasingly, some parties are calling upon the FERC to begin to exercise its current authorities by addressing reliability issues that intersect with the commercial needs of the industry.@ *Id.*

[5]The position paper continued that Athe FERC has issued several orders requiring parties to abide by the NERC standards and parties have assented to the requirements. However, the use of FERC=s conditioning authority to enforce NERC standards has not yet been challenged.@ *Id*. at 66.

standards. Such federal legislation should grant Amore explicit statutory authority@ to the FERC. *Id*. at 25-6.

Two years after the ESR report, the Final POST report endorsed the Task Force recommendations for the development of mandatory reliability standards for bulk power systems. The POST report called for federal support for the creation of a self-regulated reliability organization with federal oversight to develop and enforce reliability standards. Final POST report at 21. Importantly, the report called for the federal government to Asupport the creation of a self-regulated reliability organization with federal oversight to develop and enforce reliability standards for bulk-power systems as part of a comprehensive plan for restructuring the electric industry.@ *Id.* In explaining its recommendation, the report continued that the federal government should Aauthorize@ the creation of an industry-self-regulated reliability organization. The Alliance believes that such authorization must be accomplished through comprehensive federal legislative action.

B. Any Action By FERC To Establish Mandatory Reliability Rules Through Rulemaking Would Be A Marked Departure From The Commission=s Past Practice.

FERC=s own view is that its direct authority over reliability issues is limited. As recently as May 2000, the Commission stated that it Adoes not have direct responsibility over reliability matters.@[6] Rather than setting reliability rules itself, as would be expected were the Commission to undertake a reliability rulemaking, the Commission=s Ahistorical position has been that the responsibility for establishing mutually acceptable operating practices falls, in the first instance, on the owners and operators of the interconnected system.@ *Western Systems Coordinating Council*, 87 FERC & 61,060 at 61,234 (1999)(citations omitted)(hereafter referred to as *WSCC*).

[6] *Notice of Interim Procedures to Support Industry Reliability Efforts*, 91 FERC & 61,189 at 61,673 (2000)(A*Notice of Interim Procedures*@).

The Commission explained its role in reliability matters in *WSCC*. There the Commission accepted for filing the WSCC=s proposed Reliability Management System (ARMS@), applying a Arule of reason@ to determine that the RMS Asignificantly@ affected the Commission=s jurisdiction. While recognizing that there is an Ainfinitude of practices affecting rates and service,@ only those with significant impacts would be subject to Commission scrutiny. 87 FERC at 61,233 (citations omitted). The Commission explained that:

> [i]n agreeing to accept the RMS for filing we wish to make clear that we do not intend to assume the role the regional reliability groups have traditionally performed in developing

> reliability criteria. Instead, we will consider such criteria only to the extent needed to fulfill our traditional role of ensuring that rates, terms and conditions of *jurisdictional service*, as distinct from reliability criteria, satisfy FPA requirements.

87 FERC at 61,234 (emphasis in original, citations omitted). The Commission indicated that it would give Asubstantial deference@ to WSCC in reliability matters, and would take a Alimited role in resolving disputes about failures to adhere to the WSCC reliability criteria,@ in part because of the Commission=s Alimited experience on the issues addressed by the RMS.@ *Id*.

The Commission has disclaimed any interest in becoming involved in the day-to-day operations of the electricity grid.[7] Rather, the Commission has, properly, expressed its commitment to exercising its regulatory responsibilities Ain a manner that supports, and does not impede, efforts to enhance reliability throughout the industry.@[8]

These statements by the Commission are particularly instructive as the Department considers whether the Commission should be asked to undertake a reliability rulemaking. Diverging at this point from the historical restraint demonstrated by the Commission when it comes to reliability matters to put FERC squarely in the position of developing reliability rules, without first expanding the Commission=s statutory authority, would be inconsistent with the careful attempts the Commission has made to limit its incursion into technical and operational

[7] *Notice of Interim Procedures*, 91 FERC at 61,674. In a concurring opinion in this case, Commissioner Hebert wrote that A[r]ealizing that the issue of reliability is complex and requires intimate familiarity with local facilities and institutions, the Commission historically has left this matter to industry-led groups, working in concert with all affected stakeholders.@ *Id*. at 61,677. Commissioner Hebert also wrote that the Commission Ahas interceded only when its review of reliability-based practices was necessary to ensure the availability and quality of open access transmission service.@ *Id.*

reliability issues. The limitations already recognized by FERC demonstrate the need for additional Congressional direction before further regulatory steps are pursued.

[8] *Notice of Interim Procedures*, 91 FERC at 61,674.

IV. Conclusion

Preservation of the reliability of the bulk power system must be a cornerstone of the transition to a more competitive electricity market. Creating an organization to develop mandatory reliability rules and providing for Federal oversight and enforcement of such mandatory rules is a key step, but is not an end in itself. New reliability rules alone will not be enough to assure that the lights stay on.

Legislative authorization for the creation of a new reliability regime must be coupled with other measures needed to speed the development of workably competitive electricity markets. Reliability measures cannot be isolated from the other steps needed to assure functional electricity markets across the nation, such as the development and implementation of properly designed economic incentives which encourage infrastructure enhancement and improve reliability. While a reliability rulemaking by FERC is not indicated, FERC can and should exercise its existing authority to provide reliability-enhancing economic incentives. The combination of such incentives and mandatory reliability rules would provide a potent formula for addressing the industry-s reliability concerns. Without the necessary elements to spur investment in infrastructure --to build, operate and maintain both generation and transmission -- relying upon a set of mandatory reliability rules could prove embarrassing and empty when it comes to pass that such rules alone will not solve the reliability problem.

Respectfully submitted,

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